ECONOMICS TIMES N.D 4/5/18

BETTER PRODUCT MIX The Street is pricing in a volume growth of 10% in FY19 & FY20 on improved supplies to MHCV segment and new OEM deals with two-wheeler makers

New Capacity in Place, CEAT More Attractive to Investors

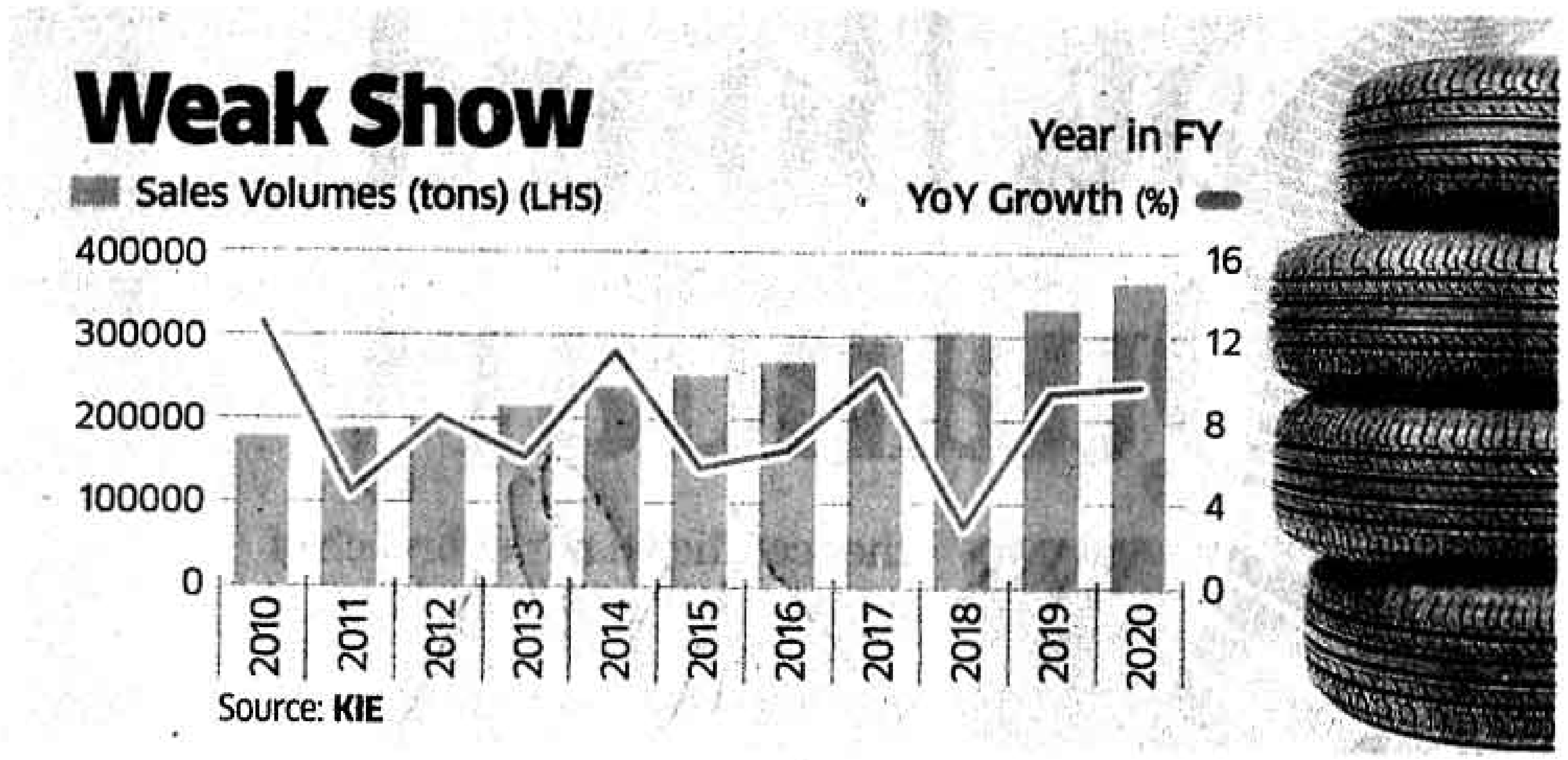
Ashutosh.Shyam@timesgroup.com

ET Intelligence Group: Volume growth and a product mix capable of underpinning superior margins should drive earnings at tyre maker CEAT, the stock of which has underperformed the benchmark Sensex in the past three months.

Sales at CEAT rose 2.9% to 304,353 tonnes in FY18, compared with the last five-year average of 7.94%. Also, the product mix weakened in the past fiscal year. Revenue growth from sales to automakers — known as OEM sales in the technical parlance — grew 27%. The OEM segment is a low-realisation business.

On the other hand, the high-margin replacement revenue rose 5%, and export revenue dropped 7% in the previous fiscal year. This restricted overall revenue growth to 8% in FY18.

The Street is pricing in volume growth of 10% in both FY19 and FY20. The commissioning of new capacity for Truck Bus Radials (TBR) at Halol-3 is scheduled from the third quarter of FY19. The new facility will be having total capacity of 210 tonnes per day, and full utilisation will be reached by 2021.



Ceat could not benefit from tailwinds in the medium and heavy commercial vehicle (MHCV) segment in FY18 amid buoyancy in the OEM and replacement volumes and a steep decline in Chinese imports. That was mainly due to capacity constraints and a weak presence in the TBR segment. Supplies from the new plant will improve the positioning of the company in the MHCV segment that contributes nearly one-third of Ceat's revenue.

On the personal mobility segment, efforts to increase market share should translate into higher revenue growth. The company is targeting a share of 15% in the next 4-5 years from 10% now.

It has launched fuel-efficient and long-lasting tyres that claim to improve mileage by 7% and run one lakh kilometres. Analysts expect revenue share of the passenger car segment to increase 15% and 17%, for FY19 and FY20, respectively, from 14% in FY18. Also, the two- and three-wheeler markets have witnessed increased competitive intensity, with the entry of new players restricting the scope for raising prices.

Ceat is offsetting the impact by adding new customers. In the March quarter, it started making tyres for four new two-wheeler models — Bajaj Pulsar 150, Honda Livo, Honda Shine and Honda Yuga. According to Kotak Institutional Equities estimates, revenue from two and three-wheeler segments is expected to grow 12% and 8%, respectively, in FY19 and FY20.

A sub-optimal product mix and lower volumes resulted in operating margins shrinking to 10.2% in FY18 from 11.6% a year ago. However, an improved product mix and cost controls should boost margins in FY19.